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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
	)	

REPLY COMMENTS

TELEPORT COMMUNICATIONS GROUP INC.

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January 10, 1997

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REPLY COMMENTS OF TELEPORT COMMUNICATIONS GROUP INC.

Teleport Communications Group Inc. ("TCG") hereby offers the following reply comments in response to the initial comments herein. TCG's comments are organized in the same format as the Joint Board's Recommended Decision.

I. INTRODUCTION.

Over the past four years, the issue of universal service has generated three FCC proceedings, numerous state proceedings, tens (and perhaps hundreds) of thousands of pages of comments, reply comments, testimony, briefs, and policy papers. With this final round of rely comments, however, resolution of this very complex issue is within sight. The Recommended Decision put forth by the Federal-State Joint Board on November 8 of last year is eminently fair and equitable, as well as legally and economically sound. The Board's proposal allows the industry and consumers to move forward, confident that universal service will be provided in a fair and efficient manner throughout the nation.

Despite the Board's well-reasoned proposal, there are those who seek to restrict or to deny the opportunity of all consumers to choose someone other than the incumbent local exchange carrier as their local telecommunications provider. In the reply comments that follow, TCG addresses those meritless arguments. In addition, TCG joins those seeking clarification of the RFP requirement for schools and libraries as it effects existing contracts, as well as the mechanism for collecting contributions from carriers.

II. DISCUSSION.

A. Principles.

It is no surprise that the Joint Board's proposal to add the principle of competitive neutrality was widely embraced and endorsed by a broad range of industry participants.[1] It is disappointing (although perhaps no less surprising) that this principle could be construed by some incumbent local exchange carriers to mean regulatory symmetry: i.e., regulations should treat new entrants as if they were incumbent monopolists, and vice versa.[2] Proponents of this view contend that incumbent local exchange carriers are at a competitive disadvantage because they have the obligation to serve as carriers of last resort, and are subject to price and service quality regulations They conveniently ignore the fact that regulation is intended to prevent exploitation of captive customers by unscrupulous telephone monopolies, and with good reason.

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[1]See, e.g., Comments of TCG, National Cable Television Association, Cox, Association for Local Telecommunications Services, AT&T, MCI, GTE, Ameritech, NYNEX, and SBC.

[2]See, e.g., Comments of GTE, SBC, Ameritech, and Pacific Telesis.

First, the incumbent monopolies have deployed ubiquitous networks funded by their captive ratepayers, and 100% of the residential telecommunications consumers remain tethered to those networks.

Second, the financial risks faced by the incumbent monopolists have been and will continue to be minimal because facilities-based competition (the only real threat to LEC revenue streams) will take time to develop. To the extent that competitors are able to win customers from the incumbents in the interim, they will generally have no alternative but to purchase some components of the incumbent's network at prices that will amply compensate the incumbent.

Third, no local telecommunications competitor is going to succeed by offering service inferior to that of the incumbent provider at prices greater than the those of the incumbent provider. The incumbents will dominate the local exchange environment for some time and it is unreasonable, indeed ludicrous, to suggest that entrants will have any market power.[3] The Commission should reject, therefore, any attempt to twist the laudable principle of competitive neutrality into an excuse to deregulate the incumbent monopolists or to regulate nascent competitors.

B. Definition of Services.

A number of parties have taken issue with the Board's recommendation not to fund service beyond the first line to the primary residence.[4] These parties

[3]See also Comments of NCTA at 13.

[4]See, e.g., Comments of GTE, U S West, SBC, and Pacific Telesis.

argue that such restrictions are unenforceable barring extraordinary policing efforts. TCG does not deny that the task of establishing procedures to audit support payments to ensure that they are supporting only the first line to a primary residence will be difficult. But there are feasible ways to do this. TCG suggests that the Commission simply require that customers in high cost areas certify that the service is for the primary residence and that the telephone number is the customer's primary listing. This would identify, as NYNEX has suggested, the customer's primary local exchange carrier eligible for universal service support.[5] Periodic audits of sample customers by the fund administrator (or by a some other entity designated by the Commission) would discourage fraud. The Commission should not countenance misuse of universal service support simply because it may be impossible to identify and punish every instance of fraud. The Commission must take whatever reasonable steps necessary to minimize fraud and abuse and to maximize the effectiveness of the program.

TCG also reiterates its position that the universal service fund should not support service to single-line businesses.[6] In addition to the reasons we enumerated in our original comments, we draw attention to an excellent point identified by Ameritech: because expenditures for telephone service are tax

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[5]See Comments of NYNEX at 6.

[6]See Comments of TCG at 3-4.

deductible expenses for most small businesses, additional support from the universal service fund is unnecessary.[7]

C. Rural, Insular, and High Cost Areas.

TSLRIC Principles and Embedded Costs

A number of parties have suggested that adherence to the cost principles of Total Service Long Run Incremental Cost ("TSLRIC") will prevent the incumbent local exchange carriers from recovering their "actual" costs of providing universal service. They argue further that competition will prevent them from recovering the cost of their undepreciated investments in plant and equipment. They propose instead to base the cost of basic service on the accounting costs of the incumbent LECs and to allow the incumbents to recover their undepreciated investments via the universal service fund.

GTE, for example, contends that "[i]n any competitive market, in order for the market to be in equilibrium, the average price in the market must cover the actual average cost of the providers in the market. Today, in the local exchange market, those providers are the ILECs."[8] The problem with this statement is that there is no local exchange "market," and the ILECs are not providers in a competitive market. They are monopolists that have been subject to a variety of regulatory regimes over many decades, none of which could ever be construed as replicating the incentives of a competitive market. Therefore, contrary to Pacific

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[7]See Comments of Ameritech at 7.

[8]See Comments of GTE at 26.

Telesis's comments,[9] there is every reason to believe that the LECs have failed to build networks in an efficient, cost effective manner.

Because no competitive market exists for basic service, the ILECs' cannot be presumed to be the most efficient, least cost providers. TCG strongly urges the Commission to adopt the Board's recommendation to determine the cost of basic service according to a proxy model that reflects the true TSLRIC of basic service. TCG is confident that the cost study workshops to begin in January will produce a model that will generate a proper estimate of the true cost (i.e., TSLRIC) of basic service.[10]

D. Schools and Libraries.

Both TCG and the Education and Library Networks Coalition ("EDLINC") expressed concern regarding Paragraph 572 of the Recommended Decision.[11] As TCG noted, Paragraph 572 seems to indicate that a school or library with an existing contract with the incumbent local exchange carrier does not need to open that contract to competitive bidding in order for the carrier to receive universal service funding. In our view, this contradicts the reasonable and prudent RFP requirement of paragraph 539.

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[9]See Comments of Pacific Telesis at 11.

[10]TCG also urges the Commission to reject consideration at this time of GTE's auction proposal. As indicated in the attached *ex parte* letter from TCG to the Joint Board filed last October, auctions are too complex and are inappropriate in the current ILEC-dominated environment.

[11]See Comments of TCG at 8-10; EDLINC at 19.

TCG strongly believes that it is well within the Commission's authority to predicate fund distribution on the completion of an RFP. The Act authorizes support in response to a "bona fide request" for service and the Commission is both justified and authorized to establish the criteria for a bona fide request.[12] Absent such a requirement, schools and libraries would remain captives of the incumbent local exchange carriers, and competitors would be shut out of a potentially lucrative market. Should a school or library wish to take advantage of the universal service funds for which it is eligible, therefore, the Commission is justified in requiring the institution to terminate its existing contract with the incumbent local exchange carrier without penalty, to issue an RFP, and to entertain competitive bids for contract.[13] As TCG noted in our original comments, such a requirement would not apply to existing contracts that were awarded via bona fide RFPs. The Commission must require the carrier or the school, however, to provide proof that the contract was awarded via a bona fide RFP.

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[12]See 47 U.S.C. § 254(h)(1)(B).

[13]Because universal service funds will be involved, the Commission clearly has the authority to compel a "fresh look" for existing contracts for intrastate telecommunications services as a condition of receiving federal support. A school or library, for example, that does not qualify for funding or that does not want funding would be free to retain their existing contracts with the incumbent monopolist.

E. Administration.

Contributions

TCG has long supported requiring telecommunications carriers to contribute to universal service according to their share of the market as measured by gross revenue less payments to other carriers (also known as Net Transmission Revenue). We supported this approach because we believed all carriers had a responsibility to contribute to universal service, and this was the most efficient means of assessing their contributions.

After careful consideration, however, TCG is convinced that despite its many positive features, the "Net Transmission Revenue" approach might have unforeseen distorting effects on the telecommunications industry. As an alternative, therefore, TCG supports a percentage surcharge on all retail end user bills for interstate and intrastate telecommunications services. In addition to minimizing market distortions, the surcharge has the added benefit of being visible to the end users, who are the ultimate source of funding under any assessment mechanism. Given the broad social effects of the nation's universal service policy, TCG agrees with Commissioner Schoenfelder of the Joint Board, that "consumers are entitled to be made aware of the charges that they are paying to support the recommendations [of the Joint Board]."[14]

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[14] See Separate Statement of Commissioner Laska Schoenfelder, November 7, 1996.

III. CONCLUSION.

TCG has appreciated the opportunity to participate in the development of universal service policy at both the Federal and state levels in recent years. We urge the Commission to stay the course charted by Congress and to adopt the Joint Board's proposal, with the clarifications that TCG has suggested.

Respectfully submitted,

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January 10, 1997

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STAMP. & RETURN

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October 18, 1996

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OFFICE OF SECRETARY

VIA HAND DELIVERY
William F. Caton, Acting Secretary
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1919 M Street, N.W.
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Washington, D.C. 20554

Re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45

Dear Mr. Caton:

Teleport Communications Group Inc. ("TCG") hereby gives notice of an _ex parte_ presentation in the above-referenced proceeding. On October 18, 1996, Paul Cain of TCG sent the attached letter by hand-delivery to Chairman Hundt, Commissioner Quello, Commissioner Chong and Commissioner Ness. The letter was also hand-delivered to John Morabito and Geanine Poltronieri of the Common Carrier Bureau. The letter was sent by first-class mail to Sharon Nelson, Kenneth McClure, Julia Johnson, Martha Hogarty and Laska Schoenfelder, the state members of the Federal-State Joint Board.

Very truly yours,

Paul Cain

Paul Cain
Director, Government Affairs
and Public Policy
(718) 355-2255

Attachment
cc: Chairman Reed E. Hundt
Commissioner James H. Quello
Commissioner Rachelle B. Chong
Commissioner Susan Ness
Commissioner Julia Johnson
Commissioner Kenneth McClure
Commissioner Sharon Nelson
Commissioner Laska Schoenfelder
Martha Hogarty
John Morabito
Geanine Poltronieri

TCG

Regulatory Affairs

October 18, 1996

VIA HAND DELIVERY

Chairman Reed E. Hundt
Commissioner Rachelle B. Chong
Commissioner Susan Ness
Commissioner Sharon Nelson

VIA FIRST-CLASS MAIL

Commissioner Ken McClure
Commissioner Julia Johnson
Commissioner Laska Schoenfelder
Ms. Martha Hogarty

Re: Federal-State Joint Board On Universal Service
CC Docket No. 96-45

Dear Joint Board Members:

TCG strongly recommends that the GTE's proposal for auctions as a means of establishing support levels in high cost areas be rejected. Contrary to GTE's assertions in their formal comments to the FCC and in their recent comments to the press and others, their auction proposal is indeed a barrier to entry, and it is less efficient and more complex than any alterative.[1] Like most parties to this proceeding, GTE supports the use of cost studies to establish the initial subsidy level.[2] Under GTE's proposal, however, only the incumbent local exchange carriers would receive the initial subsidy amount. For a competitor to qualify for support, according to GTE, it must first engage in a bidding war with the incumbent and any other carrier wishing to serve an area. This approach is blatantly anticompetitive, and in this proceeding auctions should be prohibited except under very unusual circumstances, as discussed below. A more reasonable approach, and one that is competitively neutral, is to allow all providers access to the universal service support on identical terms and conditions.

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1. In its order rejecting GTE's auction proposal in California (R.95-01-020 and I.95-05-01-021), the California Public Utilities Commission stated that ". . . auctions for all high cost areas would be administratively difficult. The Commission or its designee may have to become involved with numerous, ongoing auctions."

2. Since filing their initial comments in this proceeding, however, GTE has apparently suggested that auctions would replace cost studies entirely, even in the establishment of the initial support level.

Adjustments to the support level will be made following periodic reviews of the rates charged for basic service by all carriers in an area. This approach is simpler, more efficient, and requires less regulatory intervention than GTE's proposal.

As discussed in TCG's comments in this proceeding, the completion of one accurate cost study is necessary for the purposes of establishing the initial funding requirement of the universal service mechanism.[3] (In the past, GTE has agreed with TCG and most other parties regarding this element of the NPRM in this proceeding. As noted above, their position may have changed.) Contrary to GTE's suggestion, however, neither auctions nor additional cost studies will be necessary to adjust the funding requirement as competition develops. As TCG detailed in its comments, once the initial support ceiling is established, only periodic reviews of the rates and services offered by providers of basic service will be necessary to determine a new funding requirement based on the average rates charged by all carriers serving an area. Such reviews could be undertaken as frequently as determined to be necessary. TCG recommends that such reviews be completed every three years (or more often as market conditions dictate), both to monitor the impact of competition and to adjust the support requirement. Simply by periodically monitoring the rates charged by competing carriers, the Commission can obtain all the information it needs to adjust the funding requirement to reflect the impact of competition on reducing the subsidy requirement. Such reviews can be completed with a minimal commitment of the Commission's or Joint-Board's resources or the resources of the carriers.

Auctions, on the other hand, are by definition, difficult to design, cumbersome and expensive to administer, and useful only under special circumstances. One need only examine the recent auction of the wireless spectrum for PCS to get an idea of the time and resources necessary to conduct an auction successfully. The PCS auction took months to design and more months to complete, and required constant and considerable oversight by the Federal Communications Commission. GTE's proposal is just as complex and the complexity is compounded by necessity of conducting multiple auctions throughout the year.

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3. GTE, however, supports a return to the long-discredited backward-looking cost studies based on embedded cost, rather than forward-looking economic cost studies.

For example, GTE would require the completion of five steps even before the carriers submit their first bid! And each step in itself represents a considerable administrative burden on both the Commission and the carriers each time an auction is conducted! The GTE proposal requires that each time the Commission contemplates a change to the funding level (and GTE recommends that the auctions be conducted as often as twice each year), it would have to identify the geographic boundaries of the auctions and would have to establish bidding schedules ("step 1"). The process is further complicated by carrier requests to adjust the auction boundaries ("step 3"), creating the possibility of seemingly endless adjustment of the auction parameters. Furthermore, GTE would require the Commission to verify each carrier's (unspecified) "eligibility requirements" not only once ("step 2") but twice ("step 4") each time an auction is undertaken. Not only could such requirements create unnecessary barriers to entry for some firms, it might also create an overwhelming administrative burden for the Commission. Even before the bids are submitted, GTE's "timeline" lays the foundation for an administrative quagmire that is as unnecessary as it is complicated.

While appropriate for the special circumstances of the wireless spectrum and potentially unserved areas, auctions cannot be completed quickly enough or cheaply enough to satisfy the industry's need for a rapid, efficient, and fair universal service adjustment mechanism. Insofar as the purpose of the auction is to reveal the value of the services provided to customers in a particular area, such information will be revealed in the marketplace in the prices charged to customers by both CLECs and incumbent LECs. An auction would only be redundant, expensive, and a substantial barrier to competition.

Sincerely,

Paul Cain

Paul Cain
Director, Government Affairs
and Public Policy
(718) 355-2255

cc: Commissioner James H. Quello
John Morabito
Geanine Poltronieri

<u>CERTIFICATE OF SERVICE</u>

I, Lois Mitchell, do hereby certify that a copy of the foregoing Reply Comments was sent by first class United States mail, postage prepaid, this 10th day of January, 1997, to the following:

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